Weekly Market Review

By: Joe Clark, CFA, Allegheny Research Team

The Week Ending March 12, 2021

The week's theme changed during Friday trading after President Biden signed a record $1.9 billion stimulus bill into law and gave an optimistic speech on the U.S. economy. The President moved up the goalposts on his "return to normal" plan, which increased optimism for higher U.S. GDP growth, and sent the 10-year U.S. Treasury bond to its highest rate in more than a year, although that high is still a relatively low 1.64%. As a result, stocks that will benefit from the economy reopening and higher rates continued to rise, while high growth stocks were unnerved to end the week.

Why is an increase in rates caused by an optimistic outlook on the U.S. economy putting pressure on technology stocks? It all comes down to how investors calculate the future value of stocks. Stocks are valued using discount rates, which are based on U.S. Treasury rates. Lower yields correlate to higher future cash flows, making investors more comfortable paying higher valuations today in return for a higher value of cash flows in the future. This has been the case for growth stocks, especially technology stocks, over the past year. Low rates continued to support expensive stocks, but perhaps positive news on a post-COVID world is sending the market to a rotation.

As positive outlooks for the economy continue, investors are selling safer assets to buy more cyclical stocks. U.S. Treasuries are known as the safest assets to own, so it makes sense they would be the first to be sold as investors become more comfortable taking on additional risk. As investors sell their Treasuries, the supply of these bonds increases. To create demand for the additional supply, yields rise to entice new buyers. Although fingers are pointed to inflation as a cause for rising rates, it is basic supply and demand economics that is the primary catalyst for the 10-year rate increasing.

Now that investors are selling bonds, what stocks are they buying? Some might say buy what has worked, but as we discussed, what has worked has been technology stocks, and they may not be as enticing with higher rates. So why not buy cheap stocks that have been punished over the past year or even longer in some cases? As the economy moves closer to a reopening, sectors like energy, financials, and consumer discretionary are more appealing as they are beginning to have economic and price momentum behind them. This is the same case for small-cap stocks, which are already up over 19% this year. While the weakness of technology stocks and inflation seem to dominate the headlines, remember there are still opportunities for patient investors with diversified portfolios to capture returns.

Allegheny Financial Group · Allegheny Investments

811 Camp Horne Road, Suite 100 • Pittsburgh, PA 15237
Ph: 412.367.3880 • Fax: 412.367.8353
alleghenyfinancial.com • alleghenyinvestments.com